

## Impact of service tax on hotel industry: An empirical study using listed companies of hotel and restaurant industry

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### **Abstract**

In recent budget, finance minister of india has announced 0.5 per cent hike in service tax. This increase of service tax from 14 percent to 14.5 percent resulted in to real worry for service industries growth in India. Infact, in last four year service tax increase from 10.3 percent to 14.5 percent that cause slowdown in differnt service related industries. In present study, researcher tries to identify whether there was impact of this service tax on growth of hotel and restaurant industry do exist or not using regression analysis. Using last five years growth data of 41 companies and service tax, the result of regression indicating clear cut negative relation between growth in hotel and restaurant industry and service tax. In fact, this significant relation talks lot about next year possiblity of further slow down in growth of hotel and restaurant industry due to further hike in service tax in this budget. However, result showing that only 21.8 percent variance of growth of hotel and restaurant industry was represented by the service tax, market capitalization of company and growth equity valuation. Hence, there is scope of identifying more variables that impacts on growth in hotel industry. The resercher's objective is to explain negetive impact of service tax on growth of service realted industry. Specifically, in this reserch paper focus was on growth of hotel and restaurant industry. This result can be helpful to the different stake holder of companies fall in service industry category, for taking decision in better way. It also help to government for understand negetive impact of service tax on growth of service industry that in way hurting economy as whole.

### **Keywords:**

Service Tax, Service Industry, Hotel & Resturant Industry, Market Capiatlization, Budget

## **Introduction**

The history of the hotel and restaurant industry in service management is as old as the history of tourism and travel industry. In fact, both are two sides of the same coin. Both are complementary to each other. Hotel is an establishment which provides food, shelter and other amenities for comfort and convenience of the visitors with a view to make profit (Chakravarti, B.K). However, during the last few years great changes have taken place in the scope of hotel industry. During 6th century BC, hotels were known as "inns" or "dharamshalas" were providing only food and overnight stay facilities. At that point of time the standard of an inn was quite normal with earth or stone floor, common bedroom and simple food. As travel became easier, inns grew in size and number. The spirit of competition raised the standard of inns. In fact, growth of tourism and travel industry is becomes so important that prime minister giving importance of tourism and travels with campaigning of "Incredible India".

## ***Significance***

Tourism and hospitality industry may help underdeveloped/developing countries more in resolving their various problems as this industry today has emerged as one of the fastest growing industries in terms of capital invested, foreign exchange earnings and providing jobs. In India, it is considered as highly labour intensive service industry, where the employment-investment ratio is higher than any other industry. One of the India's biggest problems is to find ways to employ its ever-growing population. Hotel and restaurant directly creates employment opportunities in hotels, restaurants and related services. As a result of the spread effect creates jobs in industries like construction, telecommunication, manufacturing and the retail trader. According to Ministry of Tourism (parental industry for hotel and restaurant industry), an investment of Rupees one million in the hotel and restaurant sector may create 89 jobs as against 44 jobs in agriculture sector and 12.5 jobs in the manufacturing sector. Investment required to create one job in manufacturing sector is around Rupees.79,000 where as in hospitality industry it is only Rupees11,200. At present about 20 million persons are directly or indirectly employed in tourism related industry and this figure is likely to increase to 40 million by 2020.

## ***Recent Trends***

At present about 789 million tourists are crossing international boarder every year and they are spending nearly 685 billion US Dollars. This figure was just 100 million in 1964. The figure is likely to swell to 1.5 billion by 2020 as per projection by world tourism organisation. International tourists here in India were 19.5 million in 2015 as against 2.78 million tourists in 2003. It is expected that this growth will continue during the next couple of years if no adverse incident happens in India or the South East Region. According to an estimate of CII, the number of foreign tourists visiting India is likely to increase to 50 million by 2020. As per estimates of Ministry of Tourism, 1,50,000 hotel rooms of different categories are required to be added to the existing available rooms in the next couple of years to accommodate all the foreign tourists and this will involve an investment of Rs. 35,000 crores. Obviously, there is a good scope for hotel business all over the world including India and these estimates will boost hotel business in India.

## ***Problems of Hospitality Industry in India***

However, as each industry facing some problems, hotel and restaurant industry isn't exception. It has problem of seasonality, problem of high Consumer Expectations, low profitability, problems of raising funds, shortage of skilled employees, retaining quality work force, shortage of rooms, intense competition and creating brand 'India', manual back-end, human resource development, large part of the industry is in unorganized sector, lost location advantage etc...

Above all, currently in last five year industry is facing problem related to high Direct and indirect Taxes. Specifically, service tax raised from only 10.3 percent to 14.5 percent and that resulted in adverse impact

on growth of hotel and restaurant industry.

### ***History of service tax***

The Service Tax was introduced in India around 21 years back on July 1, 1994 on three services at the recommendations of Dr. Raja Chelliah Committee on tax reforms. It was introduced on three services were:

1. Telephone
2. Stockbroker
3. General Insurance

The Finance Act, 1996 enlarged the scope of levy of Service Tax covering three more services. Nine more services were added by the Finance Acts of 1997 and 1998. The Union Budget 1998-99 further extended the scope of service Tax by including twelve more services. Fourteen more services were added by the Finance Act 2001. In the Budget 2002-2003, 10 more services were added to the tax net. Finance Bill, 2005 has introduced nine more services expanding the number of taxable services to eighty-one.

Not only that, service tax rate was also increased significantly in last decade. And in last five years, this increase is really slowing down some of the service related industries growth. And That is become real worry about stake holders engaged with service sector.

### ***Recent trend of service tax***

Now, consumers will pay more for various services starting November 15, 2016. In the Union Budget, finance minister Arun Jaitley had proposed to increase the service tax from 14 per cent to 14.5 per cent with name of Swachh Bharat cess. Above that, announcement is done for imposing Swachh Bharat cess up to 2 percent on any of service tax. This service tax hike, applicable from November 15 onwards, hasn't been well received by the Indian hotel and restaurant industry. According to them, the hike will adversely impact the end consumers' frequency of dining out, the number of inbound tourists to India, among others.

In summary, this problem of increase in service tax need to required to study for future growth of hotel and restaurant industry. In present study, researcher tried for the same.

### ***Review of Literature***

Global Investments in hospitality Sector has shown increasing trend over last few years. Asia is viewed as Top Global Prospect for Hospitality Investment. Emerging markets in Asia are unseating Europe as the epicenter of new hospitality investment and development while investors in the United States are switching their focus from the acquisition of existing hotels to developing new properties (Biswanath Ghosh, 1998). According to the Ernst & Young Hospitality Investment Survey, which surveyed more than 300 investors and industry executives worldwide, capitalization rates for hotel properties are expected to stabilize and possibly even increase over the short-to-mid-term in the US. Even with the dramatic shift in the debt markets over the last few months, hotel industry sector fundamentals continue to be strong. (Brian Tress of Ernst & Young's Hospitality Advisory Services Group)

Mr. Pallonjee Pestonjee is called as the pioneer of the western style hotel in India who opened the first – western style hotel under the name of British Hotel in Mumbai in 1840. By the end of the nineteenth century, many western style hotels were established in India. These hotels were very much popular for their efficient management, unsurpassed cuisine and the excellence of beers and wines. The twentieth century may be called as the beginning of star hotels in India. In this century, big and modern hotels came into existence on account of the advent of big businessmen and new entrepreneurs ( Negi Jagmohan).

As far as different factor that affects Indian hotel and restaurant industry, Kaul, R. N. (1928), Nagi J.M.S

(1982 and Aksu, A. A. (2000) had done research that shows clear impact of seasonality, size and workforce on hotel industry.

As we discuss earlier, there is clear cut negative possible impact of service tax on hotel and restaurant industry. There isn't any work found related to direct impact of service tax on hotel and restaurant industry.

However, Rajesh Chanda (2012) in his national council of applied economics research's final report clearly shown impact of service tax on service industry and international trade in India.

### ***Purpose of the Study***

Main objective is as follow:

1. Understanding impact of service tax on hotel and restaurant industry Sub Objectives are
2. To understand behavior of growth in hotel and restaurant industry due to increase in service tax
3. To understand impact of service tax, market size of company and growth of market size together on growth of hotel and restaurant industry

### **Research Methodology**

#### ***Sample Used for Analysis***

Data for total 171 listed and non listed companies were available in hotel and restaurant industry through capital line data base. Out of 171 companies only 50 companies were listed and traded currently on exchange, so that only 50 companies' market capitalization data can be extracted from data base. For these 50 companies' last six year data was checked for company revenue, market capitalization data. Only 35 companies were found live on data base for last six year. So, data from 2010 to 2016 were taken for all this 35 companies. So, for calculating the growth value 5 data points per company were considered. Thus, total  $35 * 5 = 175$  observation taken. Data for service tax for same years were taken from government website.

#### ***Methodology Used***

For check impact of service tax, market capitalization and growth of equity value on growth of hotel and restaurant industry regression analysis was used. Proposed model was as follow:

$$GRHR = a + b * ST + c * MC + d * GEV$$

Where,

GRHR = Growth in revenue for hotel and restaurant industry

ST = Service Tax

MC = Market Capitalization

GEV = Growth in equity valuation

a, b, c and d = coefficient

Hypothesis:

$H_{0(1)}$ : *There isn't any significant impact of service tax on growth of revenue in hotel and restaurant industry*

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$H_{0(2)}$ : *There isn't any significant impact of market capitalization on growth of revenue in hotel and restaurant industry*

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$H_{0(3)}$ : There isn't any significant impact of growth of equity value on growth of revenue in hotel and restaurant industry

$H_{a(3)}$ : There is significant impact of growth of equity value on growth of revenue in hotel and restaurant industry

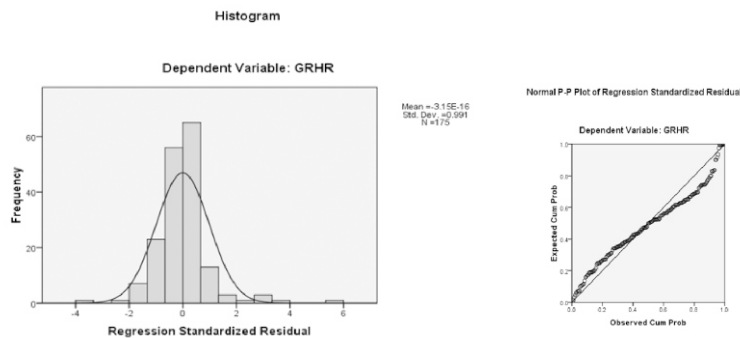
**Data Analysis and Interpretation**

Multiple regression analysis is used to study the impact of service tax, market capitalization and growth in equity value together on growth in revenue for hotel and restaurant industry. Multiple regression analysis was performed in SPSS 16.0.

The following assumption check has done before the analysis:

- Normality of the error
- Linearity
- Homoscedasticity and
- Independence of error
- No multi co-linearity between independent variables

**Figure 1: Plots for GRHR**



Source: Output from SPSS 16.0 for check normality, linearity and homoscedasticity

However, as all the available data is taken from capital line fourth assumption of independence of error considered as true. And Result of table 1 shown ANOVA model result that confirms model significant at 1 per cent level (F=15.866, p = 0.000).

**Table -1 : ANOVA<sup>b</sup>**

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	14625.654	3	4875.218	15.866	.000
Residual	52542.310	171	307.265		
Total	67167.964	174			

a. Predictors: (Constant), GEV, ST, MC

b. Dependent Variable: GRHR

Source: Output from SPSS 16.0

Thus, further analysis is carried out for understand impact of service tax, market capitalization and growth in equity value together on revenue growth of hotel and restaurant industry. Table 2 represents model summary, which clearly indicating that 21.8 percent of variance in revenue growth of hotel and restaurant industry was explained by service tax,market capitalization and growth in equity value together.

**Table 2: Model Summary**

<b>R</b>	<b>R Square</b>	<b>Adjusted R Square</b>	<b>Std. Error</b>
0.467	0.218	0.204	17.53

Source: Output from SPSS 16.0

Source: Output from SPSS 16.0

Further to understand multi co-linearity and impact of individual factor on revenue growth of hotel and restaurant industry coefficient summary was presented in Table 3. Table 3 confirms non multi co-linearity between independent variable as VIF value is between 1 and 2.

Also, it indicates that all three null hypothesis established in research methodology were rejected. So, one can interpret result as on an average 1 percent increase in service tax significantly ( $p < 0.05$ ) resulted in decrease in growth in revenue by 4.142 percent in hotel and restaurant industry. On an average 1 crore increase in market capitalization significantly ( $p < 0.05$ ) resulted in on an average increase in revenue growth by 0.018 percent. And On an average 1 percent increase in equity valuation significantly ( $p < 0.05$ ) resulted in on an average increase in revenue growth by 0.16 percent.

**Table 3 : Regression Statistics**

<b>Model</b>	<b>Unstandardised coefficient</b>	<b>Standard Coefficient</b>	<b>P-value</b>	<b>VIF</b>
a	54.468	---	0.000	
ST	4.142	-0.298	0.000	1.003
MC	0.018	0.158	0.021	1.008
GEV	0.160	0.322	0.000	1.005

Source: Output from SPSS 16.0

Model can be shown in equation form as follow:

$$GRHR = 54.468 - 4.142 * ST + 0.018 * MC + 0.16 * GEV$$

***Major findings and Implication of the study***

Result show clear positive impact of market capitalization and growth in equity value on revenue growth of hotel and restaurant industry. However, one can't have control over this variable for keep good growth of hotel and restaurant industry.

It was found that there is negative impact of service tax on revenue growth of hotel and restaurant industry. So, government need to consider this point during announcing additional direct or indirect taxes on service industry.

Recent announcement related to increase in service tax by 0.5 percent may result in  $-4.142/2 = -2.071$  percent decline in revenue growth of hotel and restaurant industry.

It was found current developed model can be explaining only 21.8 percent variation of revenue growth. So, need to identity more variable that can be controlled for growth of hotel and restaurant industry.

### **Conclusion**

In present study, research attempted to understand government policy making with special focus on service tax. It was concluded based on results of analysis that hike in service tax results in the decline in hotel and restaurant industry. On the one side, government is talking about “Incredible India” campaigning for the fast and rapid growth of tourism and hotel industry. While on the other side, government is continuously increasing service tax on service industries including hotel and restaurant industry. These resulted in overall decline in growth of revenue of hotel and restaurant industry. So, using present study research had attempted humble try for showing conflict between government campaigning and its policy. Furthermore, Announcement of this budget regarding adding 0.5 percent swachh bharat cess this year and probable increase up to 2 percent will defiantly result in to decline in growth of hotel and restaurant industry.

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